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In the Supreme Court

OF THE

United States

OCTOBER TERM, 1966

No. ~~950~~

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BANK OF MARIN,

Petitioner,

VS.

JOHN M. ENGLAND, Trustee
in Bankruptcy,

Respondent.

PETITION FOR A WRIT OF CERTIORARI

to the United States Court of Appeals
for the Ninth Circuit

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In the Supreme Court

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OCTOBER TERM, 1966

No.

BANK OF MARIN,

Petitioner,

vs.

JOHN M. ENGLAND, Trustee
in Bankruptcy,

Respondent.

PETITION FOR A WRIT OF CERTIORARI to the United States Court of Appeals for the Ninth Circuit

Petitioner, Bank of Marin, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in the above entitled case on October 28, 1965.

OPINIONS BELOW

The memorandum opinion of the District Court for the Northern District of California (R 55-56) incor-

porating the opinion of the Referee in Bankruptcy is unreported, as is the opinion of the Referee (R 112-113; Appendix A pp. xvii-xix). The opinion of the Court of Appeals for the Ninth Circuit is reported at 352 F. 2d 186 (1965). (Appendix A pp. i-xv.)

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was made and entered on October 28, 1965. (R. 121; Appendix A p. xvi.) The jurisdiction of this Court is conferred by 11 U.S.C. 47(c) and 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a Bank which honored checks of a depositor after the depositor had filed a voluntary Petition in Bankruptcy is liable to the Trustee in Bankruptcy for the amount of the checks paid, where the Bank had no notice whatsoever of the bankruptcy proceedings.

STATUTES, FEDERAL RULES AND REGULATIONS INVOLVED

The applicable portions of the Fifth Amendment of the United States Constitution, Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) and Bankruptcy Act Section 70 (11 U.S.C. 110) are set forth in Appendix B pp. xx-xxi.

STATEMENT OF THE CASE

The relevant facts are not in dispute. (R 121.) Between August 27, 1963 and September 17, 1963, Marin Seafoods, Inc., drew and delivered five checks in favor of Eureka Fisheries, Inc. on its commercial account with the petitioner Bank of Marin, San Rafael, California. The total amount of the checks was \$2,312.82. (R 121.)

On September 26, 1963, before the checks were presented to the Bank of Marin for payment, Marin Seafoods, Inc. filed a voluntary Petition in Bankruptcy in the United States District Court for the Northern District of California, Southern Division, located at San Francisco, California. (R 121.) John M. England was appointed as Receiver and acted as such until October 20, 1963, at which time he became Trustee for the Bankrupt. (R 122.)

On October 2, 1963, the checks which Marin Seafoods, Inc. had drawn and delivered to Eureka Fisheries, Inc. prior to the filing of the Petition in Bankruptcy were duly presented to the Bank of Marin by Eureka Fisheries, Inc. for payment. (R 122.) There were sufficient funds on deposit and the Bank of Marin honored the checks. At the time the Bank of Marin paid the checks it had received no notice, and had not otherwise obtained knowledge of the filing of the voluntary Petition in Bankruptcy by Marin Seafoods, Inc. (R 122.) The Bank of Marin was not informed of the pending bankruptcy proceedings until October 3, 1963, when it received a letter dated Octo-

ber 2, 1963 from the Receiver. (R 122.) This was one day after the Bank had honored the five checks.

The Trustee thereupon applied to the Referee for a Turnover Order pursuant to Section 2(a) of the Bankruptcy Act (11 U.S.C. 11(a)) seeking to require the Bank to pay over to the Trustee a sum of money equivalent to the sum it paid Eureka Fisheries, Inc. on October 2, 1963. (R 122.) In the alternative, the Trustee sought relief against Eureka Fisheries, Inc. After the ensuing Order To Show Cause proceeding, the Referee held that the Bank of Marin and Eureka Fisheries, Inc. were jointly liable to the Trustee for the sum of \$2,312.82, the amount paid by the Bank of Marin to Eureka Fisheries, Inc. (R 122.) Subsequently, Eureka Fisheries, Inc. paid the total amount of \$2,312.82 to the Trustee and then filed with the Bankruptcy Court, and served upon the Bank, a notice of payment and demand for contribution as required by California Code of Civil Procedure Section 709 (R 68, 69.)¹

¹The applicable portions of California Code of Civil Procedure Section 709 provide:

"Party Who Pays More Than His Share May Compel Contribution. When property, liable to an execution against several persons, is sold thereon, and more than a due proportion of the judgment is satisfied out of the proceeds of the sale of the property of one of them, or one of them pays without a sale, more than his proportion, he may compel contribution from the others; . . . In such case, the person so paying or contributing is entitled to the benefit of the judgment, to enforce contribution or repayment, if, within ten days after his payment, he file with the Clerk of the Court where the judgment was rendered, notice of his payment and claim to contribution or repayment. Upon a filing of such notice, the

The Bank of Marin petitioned for a review of the Referee's Order pursuant to Section 39(c) of the Bankruptcy Act (11 U.S.C. 67(c)). (R. 123.) The District Court affirmed the Referee's decision and the Bank then appealed that decision in accordance with Section 24 (11 U.S.C. 47) and Section 25 (11 U.S.C. 48) of the Bankruptcy Act. (R. 123.) The Court of Appeals for the Ninth Circuit made and entered its Judgment affirming the decision of the District Court on October 28, 1965.

The Bank has taken the position at each successive stage in these proceedings that it is not liable to a Trustee in Bankruptcy when, in good faith, and without notice of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the filing of a voluntary petition. However, the Referee, the District Court and the Court of Appeals, after having considered the question, have held that the lack of notice affords no protection to the Bank of Marin.

Clerk must make an entry thereof in the margin of the docket."

Federal Rule of Civil Procedure Section 69 provides that the process to enforce a judgment, by execution or otherwise, is that applicable in the State where the District Court is held. [See: *Schram v. Spivak* (D.C.Mich. 1946) 68 F. Supp. 451, holding that the Michigan procedure similar to that set forth in California Code of Civil Procedure Section 709 was available in Federal Court.]

California Code of Civil Procedure Section 709 enables a joint judgment debtor, who pays more than his portion, to use the judgment to enforce contribution from his co-debtor by immediate execution without the necessity of further proceedings. *Tucker v. Nicholson*, 12 C. 2d 427, 84 P. 2d 1045 (1938); *Painter v. Bergland*, 31 C.A. 2d 63, 87 P. 2d 360 (1939.).

REASONS FOR GRANTING THE WRIT

(1) The Court of Appeals has decided an important question arising under the Federal Bankruptcy Act that has not been previously settled by this Honorable Court and has not been resolved by any other Court of Appeals. The only prior reported decision was rendered by a District Court in *Rosenthal v. Guaranty Bank & Trust Co.* (D.C. La. 1956), 139 F. Supp. 730, and is in direct conflict with the decision rendered by the Court of Appeals in this case.

The issue that was presented to the Court of Appeals and which is of such importance, that it should be settled by this Court involves the interpretation and application of Bankruptcy Act Section 70 (11 U.S.C. 110) in connection with Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)).

The lower Court held that Bankruptcy Act Section 70(a) (11 U.S.C. 110(a)) vests the Trustee in Bankruptcy, by operation of law, with the title of the bankrupt to its bank deposits as of the date of the filing of the voluntary petition. Therefore, the Court reasoned, the Bank is liable to the Trustee for an amount equivalent to the amount of the checks it honored after the bankruptcy of its depositor, Marin Seafoods, Inc., even though it had no notice of the bankruptcy and was acting in good faith. In so doing, the Court of Appeals decided that nothing in Section 70(d) (11 U.S.C. 110(d)) of the Bankruptcy Act afforded the Bank protection, including the negotiability provision which provides as follows: "...

Provided, however, that nothing in this Act shall impair the negotiability of currency or negotiable instruments”.

This interpretation by the Court of Appeals of Section 70(d)(5) is erroneous and unreasonable. It eliminates from the coverage afforded by the Section the party that most frequently will be involved in a negotiation, that is, the drawee Bank.²

It is inconceivable that Congress intended, when it enacted Section 70(d)(5), to deny protection to the Bank where the bankrupt has his deposits. The drawee Bank is the party who can most seriously be injured by a bankrupt who withdraws money from his savings account or delivers checks on his commercial account after bankruptcy and before the bank has knowledge of that fact. A reasonable interpretation of Section 70(d)(5) and the one intended by Congress is explained in *Rosenthal v. Guaranty Bank & Trust Co.* (D.C. La. 1956) 139 F. Supp. 730. There the District Court, in deciding the same question that is presented here, held that the negotiability provision of Section 70(d)(5) was designed to protect a Bank, which in good faith and without actual knowledge of

²Although delivery of a check to the payee is a negotiation in many jurisdictions, a payee receiving a check so close to the moment of bankruptcy would either be a preferred creditor (Bankruptcy Act Section 60 (11 U.S.C. 96)) or a fraudulent transferee (Bankruptcy Act Section 67 (11 U.S.C. 107)) and not entitled to retain the money in any event.

the bankruptcy, honored checks drawn upon it by a bankrupt depositor.³

(2) The decision of the Court of Appeals applies Bankruptcy Act Section 70 (11 U.S.C. 110) and Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) in an unconstitutional manner at variance with the appli-

³The Court's reasoning in *Rosenthal* is set forth in the following quotation:

"The trustee particularly directs the court's attention to subparagraph (5) of Title 11 U.S.C.A. Section 110, subdivision d, which he says plainly and expressly states that except as provided in subdivision d and in subdivision g of Section 44 (which latter subdivision relates to real estate and has no bearing here), no other transfer after the date of the bankruptcy shall be valid against the trustee, and of course, he argues, the only exceptions stated in subdivision d are that the payments must be made both before adjudication and without notice of the pending proceedings.

"This argument is not without merit and were it not for the fact that there is appended to that section the proviso 'that nothing in this title shall impair the negotiability of currency or negotiable instrument', we would be inclined to agree. Since no court decision has been called to our attention, and none have been found interpreting the meaning or purpose of this provision, the matter must be considered *res integra*. When the bankruptcy occurs the bank upon which the bankrupt drew a check prior to the date of the bankruptcy finds itself caught in the intermeshing of two highly complicated systems of law. Traditionally, it is the primary function of the Bankruptcy Act to protect the creditors, to marshal the assets, and to distribute them among creditors equitably and ratably in accordance with their respective rights and interests. Negotiability tries to give the bank the maximum assurance that it will be able to cash the check without any defenses being interposed. An expansion of bankruptcy in some senses indisputably hinders the flow of commercial paper. In the absence of any prior interpretation, we agree with counsel for defendants that one of the purposes of the 'negotiability' provision in the Bankruptcy Act was to protect a bank in a case of this kind, if the bank was in good faith and had no 'actual knowledge' of the pending bankruptcy." (*Rosenthal v. Guaranty Bank & Trust Co.* (D.C.La. 1956) 139 F. Supp. 730 at p. 734.)

cable decisions of this Court relating to the necessity of notice prior to imposing liability upon a party.

The due process clause of the Fifth Amendment forbids imposing liability unless reasonable notice of the proceeding is given. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 94 L. ed. 865, 70 S. Ct. 652 (1949); *Lambert v. California*, 355 U.S. 225, 2 L. ed. 2d 228, 78 S. Ct. 240 (1957); *Walker v. Hutchinson*, 352 U.S. 112, 1 L. ed. 2d 178, 77 S.Ct. 200 (1950). The due process clause also prohibits imposing liability where to do so would require the payment of a single debt twice. *Western Union Telegraph Co. v. Pennsylvania*, 368 U.S. 71, 7 L. ed. 2d 139, 82 S. Ct. 199 (1961); *Huron Holding Corp. v. Lincoln Mine Operating Co.*, 312 U.S. 183, 85 L. ed. 725, 61 S. Ct. 513 (1941).

The lower Court's decision is clearly in conflict with the broad principles set forth in *Mullane v. Central Hanover Bank & Trust Co.*, *supra*, regarding the necessity of adequate notice. This Court held in *Mullane* that due process demands that the deprivation of property by adjudication be preceded by notice and an opportunity for hearing. Adequate notice was defined as being that which is reasonably calculated under all the circumstances to apprise the interested parties of the action and to afford them an opportunity to present their objections. The Court of Appeals concedes that no notice was given the Bank. It further states that the Bankruptcy Act does not require that notice precede imposing liability upon the Bank. Such a decision is patently

inconsistent with the well established principles set forth by this Court.

The lower Court erroneously attempted to distinguish the notice requirements of due process as set forth in *Mullane* by taking the position that all that is required is that the Bank have notice of the hearing on the Turnover Order as opposed to notice of the adjudication of bankruptcy. Such a distinction is without merit. The Bank's rights and duties were fixed at the time of the adjudication of bankruptcy of which it had no notice. This was the point in time where the Bank's obligation was shifted from the bankrupt to the Trustee. It is this proceeding that is the relevant one and the one of which the Bank is entitled to receive reasonable notice before its rights can be affected.

The Court of Appeals avoided the second due process issue presented by the Bank. This Court has on numerous occasions stated that there is a strong constitutional policy against requiring double payment of the same debt. (See: *Western Union v. Pennsylvania*, 368 U.S. 71, 7 L. ed. 2d 139, 82 S. Ct. 199 (1961); *Huron Holding Corp. v. Lincoln Mine Operating Co.*, 312 U.S. 183, 85 L. ed. 725, 61 S. Ct. 513 (1941)). The lower Court's decision is clearly contrary to the expressions of this Court in that regard.

It is conceded that the relationship of a Bank to a depositor is that of a debtor and creditor and that the Bank is obligated to discharge its indebtedness by honoring checks drawn by its depositor. Failure to

honor such checks results in liability to the depositor. (See: *Weaver v. Bank of America*, 59 C. 2d 428, 380 P. 2d 644 (1963); *Reeves v. First National Bank*, 20 Cal. App. 508, 129 Pac. 800 (1912); *Allen v. Bank of America*, 58 Cal. App. 2d 124, 136 P. 2d 345 (1943)). The Bank in honoring the checks was properly discharging its indebtedness in accordance with its obligation to its depositor. The decision of the Court of Appeals now requires the Bank to satisfy its obligation again, this time to the Trustee.

The Court of Appeals disregarded the due process problem by holding that as of the moment of the filing of the petition, the Bank's duty with regard to the deposit was owed to the Trustee, not to the bankrupt, and consequently the Bank, in honoring the checks, was not satisfying an obligation. The Court of Appeals did not deal with the crucial issue involved, that is, whether the Bank's obligation could be transferred from the depositor to the Trustee without giving the Bank notice of the fact and that lacking such notice, the Bank can be held liable if it honored its depositor's checks in good faith. The basic principles established by the Supreme Court demand that the Bank be informed that it no longer is obligated to its depositor before it can be held responsible to the Trustee under such circumstances.

(3) The question presented is of great economic importance to the banking industry, whose interest is evidenced by the fact that the California Bankers Association filed an amicus curiae brief with the Court of Appeals. The decision of the lower Court

will apply to commercial and savings accounts in banks and savings and loan associations. By considering the vast number of checks that are honored and withdrawals that are made daily throughout the United States in conjunction with the substantial number of Petitions in Bankruptcy that are filed daily in every District Court, the true magnitude of the economic burden that has been placed upon banks and other depositories becomes apparent.⁴

⁴The Court of Appeals stated that it felt that the problem before it was not of significant economic importance because of the fact that the *Rosenthal* case, *supra* (D.C.La. 1956) 139 F.Supp. 730 and this case, were the only reported decisions dealing with the particular problem. This is not a correct statement and is easily explained. Prior to the enactment of Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) in 1959, there was a time lag between the time of the filing of a voluntary petition and the adjudication of bankruptcy. During this period banks were protected by Bankruptcy Act Section 70(d) (11 U.S.C. 110(d)). Section 70(d) in this regard incorporated what has been well settled case law prior to 1938, the date of the enactment of Section 70(d). (See: *Citizens National Bank v. Johnson* (6th Cir. 1923) 286 Fed. 527; *Matter of Retail Stores Delivery Corp.* (D.C. N.Y. 1935) 11 F.Supp. 658.)

Although no formal notice was given, a bank would receive notice of the proceeding prior to the actual adjudication informally from the receiver or trustee just as the Bank of Marin ultimately received notice in this proceeding. Since banks actually became aware of the bankruptcy before adjudication, and had an opportunity to protect themselves, the question presented here did not arise.

However, Bankruptcy Act Section 18(f) (11 U.S.C. 41(f)) made adjudication coincidental with the filing of a voluntary petition. With the time lag eliminated, the period during which banks received actual notice and took steps to avoid liability was removed.

The enactment of Section 18(f), which was an amendment to former Section 18(g), was intended to effect only a procedural change brought about because prior to the amendment the district Judge was required to hear all voluntary petitions and to make the adjudications or dismiss the petition. Adjudication became a matter of course since there were no issues to be presented. In order to simplify the process, adjudication was then made automatic upon the filing of a voluntary petition. (See: House Report No. 241 on H.R. 4692, 86th Congress First Session (1959) 1, 2.)

Although the Court of Appeals points out that there is virtually no feasible method by which the Bank may acquire timely notice of the bankruptcy of a depositor and protect itself, the Court of Appeals states that the burden of incurring such liability should be placed on a bank even though it is the only party to the transaction who is acting in good faith.⁵ Surely, this was not the intention of Congress when it enacted Section 70 of the Bankruptcy Act (11 U.S.C. 110) nor was it intended to be the result of the amendment to Bankruptcy Act Section 18(g) (11 U.S.C. 41(g)).

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the Petition For A Writ Of Certiorari be granted.

Dated, San Rafael, California,
January 19, 1966.

CARLOS R. FREITAS,
FREITAS, ALLEN, MCCARTHY & BETTINI,
Attorneys for Petitioner.

⁵A bankrupt is obviously aware of the ramifications of his act. The transfer to the payee would either be avoidable preference (Bankruptcy Act Section 60 (11 U.S.C. 96)) or a fraudulent transfer (Bankruptcy Act Section 67 (11 U.S.C. 107)).

(Appendices A and B Follow)

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Appendix A

**United States Court of Appeals
for the Ninth Circuit**

Bank of Marin,

vs.

Appellant,

**John M. England, Trustee in Bank-
ruptcy in the matter of Marin Sea-
foods, Inc. and Eureka Fisheries,
Inc.,**

No. 19,776

Appellee.

[October 28, 1965]

**Appeal from the United States District Court
for the Northern District of California
Southern Division**

**Before: Hamley, Jertberg and Merrill, Circuit Judges
Hamley, Circuit Judge:**

Bank of Marin appeals from a district court judgment affirming an order of a referee in bankruptcy holding the bank and Eureka Fisheries, Inc., jointly liable to a trustee in bankruptcy for the sum of \$2,312.82. The sole question presented is whether a bank which honored checks of a depositor after the

depositor had filed a voluntary petition in bankruptcy is liable to the trustee in bankruptcy for the amount of the checks paid where the bank had no notice of the bankruptcy proceeding.

The relevant facts are not in dispute. Between August 27, 1963, and September 17, 1963, Marin Seafoods drew and delivered five checks in favor of Eureka Fisheries upon its commercial account with Bank of Marin, San Rafael, California. The total amount of the checks was \$2,318.82. On September 26, 1963, before these checks had been presented to the bank for payment, Marin Seafoods filed a voluntary petition in bankruptcy. The petition was filed in the United States District Court for the Northern District of California, Southern Division. John M. England was appointed as receiver and so acted until October 20, 1963, at which time he became trustee for the bankrupt.

On the date of the filing of the petition, sums of money in excess of \$3,200 were due and owing Marin Seafoods from customers for merchandise previously delivered. Beginning on the day after the filing of the petition, and continuing for several days, Marin Seafoods, through its principal officer, collected portions of these outstanding accounts receivable and deposited them in the company's commercial account at the bank. On October 2, 1963, the checks which Marin Seafoods had drawn and delivered to Eureka Fisheries prior to the filing of the petition, were duly presented to the bank by Eureka Fisheries for payment, and were paid.

At the time the bank paid these checks it had received no notice, and had not otherwise obtained knowledge of the filing of the petition in bankruptcy. The bank was not informed of the pending bankruptcy proceeding until October 3, 1963, when it received a letter, dated October 2, 1963, from the receiver. This was one day after the bank had honored the checks referred to above.

Proceeding under section 2(a) of the Bankruptcy Act (Act), 52 Stat. 842 (1938), as amended, 11 U.S.C. § 11(a) (1964), the trustee applied to the referee for a turnover order. The trustee sought to require the bank to pay over to the trustee a sum of money equivalent to the sum paid by the bank to Eureka Fisheries on October 2, 1963. In the alternative he sought relief against Eureka Fisheries. A show cause proceeding ensued, resulting in the entry of an order by the referee, supported by findings of fact and conclusions of law. The referee determined that the bank and Eureka Fisheries were jointly liable to the trustee for the sum of \$2,312.82, the amount paid by the bank to Eureka Fisheries.

In so ruling, the referee held that the bank's lack of knowledge of the filing of the voluntary petition in bankruptcy by its depositor Marin Seafoods, afforded the bank no protection. Eureka Fisheries paid the total amount of \$2,312.82 to the trustee and then filed with the bankruptcy court, and served upon the bank, a demand for contribution. The bank petitioned for a review of the referee's order, and on such review,

that order was affirmed. This appeal by Bank of Marin followed.

In seeking recovery of the stated amount from the bank, the trustee relied upon section 70(a) of the Act, 52 Stat. 879 (1938), as amended, 11 U.S.C. § 110(a) (1964). This section provides, in pertinent part, that, upon his appointment and qualification, a trustee in bankruptcy shall be vested "by operation of law" with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding in bankruptcy, with exceptions not here material, to described kinds of property wherever located. Among the kinds of property so described, the statute includes:

"... (5) property, including rights of action, which prior to the filing of the petition he [bankrupt] could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered: *Provided*, . . . [not here material]."

This provision of the Act, considered by itself, would appear to support the trustee's application for a turnover order against the bank. The bank, however, contends that notwithstanding this statute, it should be held that a bank is not liable to a trustee in bankruptcy when, in good faith, and without actual knowledge of the bankruptcy proceedings, it honors the checks of a bankrupt depositor in the regular course of business after the adjudication of bankruptcy. As authority for this view, the bank cites

Rosenthal v. Guaranty Bank & Trust Co., D.C. La., 139 F. Supp. 730, stating that the holding in that case is "determinative" of this appeal.¹

In *Rosenthal*, on facts quite similar to those of the case before us, the court held that the proviso of section 70(d)(5) of the Act, 52 Stat. 882 (1938), 11 U.S.C. § 110(d)(5), providing that nothing in the Act "... shall impair the negotiability of currency or negotiable instruments ..." protects a bank in such circumstances.²

As indicated by the introductory words of section 70(d), all of that subsection applies only to transactions taking place during the interval, if any, between the filing of a petition in bankruptcy and the adjudication or the taking of possession by a receiver, whichever first occurs. But, in the case of voluntary petitions in bankruptcy, such as the one before us, there is no such interval, because the filing

¹It would perhaps have been better if the bank had referred to the *Rosenthal* case as "persuasive". In the judicial scheme of things, a district court decision which has not withstood the acid test of appellate review cannot be regarded as authoritative, much less dispositive of an appeal, but it may well be persuasive.

²Section 70(d)(5) reads:

"(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

....

"(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: *Provided, however*, That nothing in this title shall impair the negotiability of currency or negotiable instruments."

of a voluntary petition operates as an adjudication. Section 18(b) of the Act, 73 Stat. 109 (1959), 11 U.S.C. § 41(b) (1964). Therefore section 70(d)(5) of the Act, relied upon by the court in *Rosenthal*, can have no application here.³

Moreover, the presentation of a check to the drawee for payment, and the payment thereof, is not a negotiation of the check.⁴ If it is not negotiation, an order declaring invalid the presentation and payment is not impairment of negotiation. Accordingly, the "negotiability" proviso of section 70(d)(5) has no application.⁵

³Earlier cases in which banks were protected in paying checks all involved payments made after filing of the bankruptcy petition but prior to adjudication. See *Citizens' National Bank v. Johnson*, 6 Cir., 286 Fed. 527; *Matter of Retail Stores Delivery Corp.*, D.C.N.Y. 11 F.Supp. 658.

⁴See *Shammas v. Boyett*, 114 Cal.App.2d 139, 249 P.2d 880, 883; *Fidelity & Deposit Co. of Maryland v. Marion Nat'l Bank*, 116 Ind. App. 453, 64 N.E.2d 583; *Aurora State Bank v. Hayes-Eames Elevator Co.*, 88 Neb. 187, 129 N.W. 279; *First Nat'l Bank v. United States Nat'l Bank*, 100 Or. 264, 197 P. 547, 555; Seligson, *Creditors' Rights*, 32 N.Y.U.L.Rev. 708, 730-31 (1957); 4 Collier, *Bankruptcy* § 70.68 at 1502-03 n. 3 (14th ed. 1964); Britton, *Bills and Notes*, 118 (2d ed. 1961). Similarly, a drawee bank which has paid the check does not become a holder in due course. *Central Bank and Trust Co. v. General Finance Corp.*, 5 Cir., 297 F.2d 126, 128-29.

⁵It should also be noted that *Rosenthal* was decided in 1956, which was prior to the enacting of section 18(f) of the Act, making the filing of a voluntary petition in bankruptcy an automatic adjudication. However, for the purpose of applying chapters I through VII of the Act, the court in *Rosenthal* treated the approval of the petition for reorganization under chapter X as equivalent to adjudication pursuant to section 102 of the Act, 52 Stat. 883 (1938), 11 U.S.C. § 502 (1964). We therefore do not regard the fact that *Rosenthal* was decided prior to the enactment of section 18(f) as a sound basis for distinguishing that case.

We conclude that the "negotiability" proviso of section 70(d)(5) does not protect the Bank of Marin under the circumstances of this case.

The bank also contends that, in California, a trustee in bankruptcy must give a bank notice of the bankruptcy by complying with section 952 of the California Financial Code before he can hold the bank liable for honoring checks of the bankrupt.

Section 952 provides that notice of an adverse claim to bank deposits may be disregarded until the adverse claimant obtains a restraining order, injunction or other court order against the bank; without such an order the bank may honor checks drawn by the depositor or allow withdrawals by him without incurring liability to the adverse claimant. The bank contends that since the Bankruptcy Act makes no provision for notice to banks, state law should apply to fill this gap. The trustee gave no notice in this case, nor did he make any attempt to comply with section 952.

A claim of this kind, made by the trustee in bankruptcy for a bankrupt depositor, is not an "adverse claim," within the meaning of such a statute. *First National Bank of Arizona v. Butler*, 82 Ariz. 361, 313 P.2d 421. Thus, even overlooking inconsistencies between section 952 and the Bankruptcy Act,⁶ the Cali-

⁶Section 70(d) of the Act removes protection from transactions where actual notice is present, while under section 952 the bank is protected even though there is actual notice if the remaining statutory steps have not been taken. The bank argues, however, that this inconsistent provision of section 952 is severable leaving "at least" a requirement of actual notice as a requisite to liability under section 952.

ifornia statute does not undermine the district court order under review.

The bank further argues that a court of bankruptcy is governed by equitable principles and, applying those principles to this case, must protect the bank from incurring liability for honoring checks of a depositor where it had no notice of the bankruptcy of the depositor.

Under the trustee's theory of the case the bank must, in order to avoid liability, keep itself informed of the possibility of bankruptcy proceedings involving a depositor. According to the bank, this will require it to keep advised momentarily of bankruptcy filings. This burden is enhanced by the fact that filing in any district court in the United States will have the same effect. The steps demanded for protection are cited as impractical and otherwise burdensome.

The bank's dilemma is real since it is under a duty to depositors to honor checks which are validly drawn; at the same time there is always the possibility that the depositor, without the knowledge of the bank, has become the subject of bankruptcy proceedings. The hardship to the bank of keeping itself apprised of developments in the bankruptcy court is contrasted with the relatively light burden that a notice requirement would place upon the trustee. The trustee or receiver, upon filing, is informed of the bankrupt's accounts and deposits; and notification by him to the bank would be relatively simple.

The trustee, however, takes the position that there would be no great hardship resulting to banks from

a ruling imposing liability in this case. It is argued that banks have a vital interest in the credit position of depositors and that banks are well equipped to evaluate, interpret and discover factors affecting the financial well-being of depositors. The trustee cites the reviewing of local legal publications as a method of keeping abreast of bankruptcies. Also the trustee feels that keeping posted outside the immediate area would not be an insurmountable burden. In addition, it is argued that the bank has assumed this risk of doing business and can easily pass the cost of surveillance on to its customers.

Upon considering the respective arguments, we think the bank makes out a strong case for hardship and impracticability insofar as the timely discovery of bankruptcy proceedings involving depositors is concerned. We are not as certain that the problem is one which threatens great and unprotectible financial liability. The fact that our case, and *Rosenthal*, appear to be the only reported cases dealing with this particular problem is some indication that it is not one which will frequently confront banks. Moreover, it would seem that the risk, such as it is, may ordinarily be taken into account as a cost of the business and financed as such.

It is true that courts of bankruptcy exercise certain equity powers.⁷ But there is no room for equitable relief of a kind which is expressly foreclosed by the

⁷Section 2(a) of the Act, 52 Stat. 842 (1938), as amended, 11 U.S.C. § 11(a); *Pepper v. Litton*, 306 U.S. 295; *Local Loan Co. v. Hunt*, 292 U.S. 234.

Act. Section 70(d)(5), quoted in note 2, above, specifically provides that "Except as otherwise provided in this subdivision and in subdivision (g) of section 44 of this title [section 21(g) of the Act] . . ." no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee.⁸ Neither subdivision (d) of section 70, nor subdivision (g) of section 21, authorize transfers of the kind involved in this case. Equitable relief which would, as against the trustee, validate the bank's transfer to Eureka Fisheries, would thus run counter to section 70 (d)(g), and is necessarily precluded.

The California Bankers Association, appearing in this court as *amicus curiae*, joins the bank in all of the contentions discussed above. It also presents the additional argument that the failure of the trustee to revoke the bankrupt's order for the payment of funds on deposit with the Bank of Marin bars the trustee from recovery against the bank.

The gist of this argument is as follows: (1) under section 70(a)(5) of the Act, a trustee in bankruptcy succeeds only to such rights as the bankrupt possessed at the time of the bankruptcy petition, and is subject to all defenses and equities which might have been asserted against the bankrupt but for the filing of that petition; (2) in California an ordinary depositor does not have title to any specific funds deposited in a bank, the relationship of bank and depositor, founded upon contract, being that of debtor

⁸The "negotiability" proviso to this subsection has already been discussed.

and creditor; (3) under that contract, a bank has both the right and duty to honor checks of its depositors properly drawn and duly presented, unless the depositor provides the bank with notice of the revocation of his order for payment prior to the time his checks are accepted by the bank; (4) absent the giving of a timely "stop payment" order such payment operates to discharge the bank's obligation, and the depositor has no right to recover the amounts paid; and (5) under the premise set forth at the outset, the trustee is subject to the same defense.

The bankruptcy of a drawer operates as a revocation of the drawee's authority.⁹ Such revocation is not dependent upon or subject to notice to the drawee, since the trustee is immediately vested with the title of the bankrupt by operation of law. The parties to a depositor's contract with a bank are chargeable with knowing this when they enter into the contract. These circumstances constitute an implied exception to the contractual obligation of the bank to honor checks unless and until a "stop payment" notice is received. The asserted bank defense based upon lack of a "stop payment" notice is therefore not available against a trustee in bankruptcy in the case of the bankruptcy of the drawer.

Finally, both the bank and *amicus curiae* contend that the district court order under review deprives the bank of due process of law as guaranteed by the Fifth

⁹*Harrison State Bank v. First National Bank*, 116 Neb. 456, 218 N.W. 92; *Guthrie Nat'l Bank v. Gill*, 6 Okla. 560, 54 Pac. 434; *Brady, Bank Checks*, 25 (3rd ed. 1962).

Amendment. Two aspects of this Constitutional argument are presented, the first being that the due process clause forbids imposing liability upon a bank unless it has received reasonable notice of the bankruptcy proceeding.

In support of this view, *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, and several other decisions are cited. In *Mullane*, the question involved was whether adequate notice was given to a person of litigation wherein his rights were being litigated. Prior to the turnover proceedings, however, the rights of the Bank of Marin were not being adjudicated in the bankruptcy proceedings before us. Up to then, the rights of the bank were not affected by any order entered by the referee; the property of the bankrupt was vested in the trustee by operation of law. The rule as to notice set forth in *Mullane* and similar cases, is therefore inapplicable here.

In *Lambert v. California*, 355 U.S. 225, also cited by the bank, the Court held a statute unconstitutional which imposed criminal liability not for an affirmative act, but for the failure of a convicted felon to register despite lack of notice of the requirement. Since the basis for the bank's liability to the trustee cannot be equated with the violation of a criminal statute, *Lambert* is not in point.

The bank also places reliance upon *Hanover Nat'l Bank v. Moyses*, 186 U.S. 181. There, a creditor asserted that he had not been adequately notified of the filing and adjudication of a voluntary bankruptcy. But, as in *Mullane* and most of the other decisions

cited by the bank, the rights of the creditor in *Moyes* were being adjudicated in the bankruptcy proceeding.

We do not believe that *Moyes* should be extended past its holding that the creditors of a bankrupt are entitled to reasonable notice of the bankruptcy proceedings.¹⁰ The filing of a bankruptcy petition has long been regarded as a *caveat* to all the world. *Mueller v. Nugent*, 184 U.S. 1, 14. Likewise, adjudication has been held to be notice to the world, thus invalidating transactions involving the debtor's property occurring after adjudication. *J.S. & J.F. Sterling, Inc. v. Birkhahn*, 3 Cir., 30 F.2d 492, 495; 4 Collier, *Bankruptcy*, § 70.66 at 1498 (14th ed. 1964).

Congress may not proceed in complete disregard of the property rights of those dealing in good faith with bankrupts. It may, however, enact legislation balancing bankruptcy objectives with the interests of those dealing in good faith with a bankrupt. Section 70(d) of the Act, we believe, demonstrates that Congress has, in this balancing process, taken into account the latter interests and has accommodated them to the extent deemed feasible having in view the desirability of speedy, economical and effective bankruptcy administration.¹¹

In our opinion, the order under discussion does not offend the due process clause, insofar as notice to the bank is concerned.

¹⁰In *Moyes* it was held that the creditor had received sufficient notice.

¹¹See *Lake v. New York Life Insurance Co.*, 4 Cir., 218 F.2d 394, 397-99; 4 Collier, *Bankruptcy*, §§ 70.66, 70.67, pages 1494-1501 (14th ed. 1964), commenting on the legislative history of section 70(d).

This brings us to the second facet of the Constitutional argument presented by the bank and *amicus curiae*. This is the contention that the due process clause prohibits imposing liability upon the bank because to do so would require the bank to pay a single debt twice. There is a strong Constitutional policy against requiring the double payment of the same debt. See *Western Union Telegraph Co. v. Pennsylvania*, 368 U.S. 71.

The argument for the bank is premised upon these propositions: the relationship of a bank to its depositor is that of debtor and creditor; the bank is obligated to discharge its indebtedness by honoring checks drawn by depositors; and failure to honor such checks results in liability to the depositor. These propositions are not challenged by the trustee for they are well established. Next the bank argues that in honoring the checks drawn by the bankrupt, it discharged its indebtedness in accordance with its obligation to its depositor. From this, the conclusion is drawn that to require a second payment now to the trustee is a violation of the Fifth Amendment.

As we have already seen, at the time the checks were honored, title to the deposits was vested in the trustee by virtue of section 70(a). From the moment of filing the petition, the bank's duty with regard to the deposits was owed to the trustee, not to the bankrupt and not to the payee of the checks. We have already held that, in legal contemplation, the filing was sufficient notice to those subsequently dealing with the bankrupt's assets. Accordingly, and regardless of

actual notice, the bank's obligation to honor the checks disappeared before it paid them. Therefore, in paying the checks when presented by Eureka Fisheries, the bank was not paying a debt for which it was obligated. It follows that if as a result of this judgment the bank pays any part of the checks, it will not be paying the same debt twice.¹²

The bank characterizes its position as analogous to a garnishee who has paid his creditor without notice of garnishment. A garnishee is not liable to the garnishor in such circumstances. *Harris v. Balk*, 198 U.S. 215. But, the analogy is inapplicable in our case because, in bankruptcy proceedings, the filing of the petition and the adjudication is deemed notice to the world, except where the Act requires more specific notice.

Affirmed.

¹²We express no opinion as to whether the bank will, in fact, have to pay any part of these checks. As noted above, the order ran against the bank and Eureka Fisheries jointly, and Eureka Fisheries has paid the trustee the full amount of the checks in question. The rights as between the bank and Eureka Fisheries have yet to be determined.

United States Court of Appeals
for the Ninth Circuit

No. 19,776

Bank of Marin,

Appellant,

vs.

John M. England, Trustee in Bank-
ruptcy in the matter of Marin Sea-
foods, Inc., and Eureka Fisheries,
Inc.,

Appellee.

Appeal from the United States District Court
for the Northern District of California,
Southern Division

JUDGMENT

This Cause came on to be heard on the Transcript of the Record from the United States District Court for the Northern District of California, Southern Division and was duly submitted.

On Consideration Whereof, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this Cause be, and hereby is affirmed.

Filed and entered October 28, 1965.

In The United States District Court
For The Northern District of California
Southern Division

In the Matter of
Marin Seafoods, Inc.
Bankrupt.

No. 74820
In Bankruptcy

ORDER AFFIRMING REFEREE'S ORDER

Bank of Marin has petitioned for a review of the referee's order in the above entitled action adjudging it jointly liable to the trustee for \$2,312.82. Petitioner argues that because of the adverse effects on the banking industry of the referee's interpretation of the statutory bankruptcy scheme and because of possible constitutional objections a contrary construction should prevail.

After a careful review of the relevant cases and authorities and a detailed evaluation of facts alleged in the briefs filed herein, this Court has concluded that under the circumstances the referee's order was proper. The findings of fact and reasoning contained in his opinion of February 24, 1964 are hereby adopted and the judgment of March 31, 1964 is hereby affirmed.

Dated, October 26, 1964.

s/ Albert C. Wollenberg
United States District Judge

United States District Court
For The Northern District of California
Southern Division

In the Matter of
Marin Seafoods, Inc.
Bankrupt.

No. 74820
In Bankruptcy

OPINION FOR ORDER

Title to the property of a bankrupt vests in the trustee as of the date of the bankruptcy petition pursuant to the provisions of section 70a of the Bankruptcy Act. Certain transactions thereafter but prior to adjudication are protected by section 70d. However, the statute places "an absolute ban on all transfers not given specific protection under the act". *Feldman v. Capitol Piece Dye Works, Inc.* (C.A. 2, 1961) 293 F. 2d 889.

No provision contained in section 70d gives any protection to a bank which after adjudication honors the checks of the bankrupt. And the recipient of such funds after adjudication merely holds property title to which is vested in the trustee.

The bank on brief questioned the summary jurisdiction of the bankruptcy court. The point is belatedly raised. Bankruptcy Act section 2(7). In any event the facts do not show the bank ever had any claim to these funds deposited with it after adjudication of the bankrupt.

The trustee is entitled to a judgment against the Bank of Marin for \$700.47 and against the Bank of Marin and Eureka Fisheries, jointly, for \$2,312.82.

The trustee shall serve and lodge appropriate findings of fact, conclusions of law and order.

Dated at San Francisco, California, this 24th day of February, 1964.

Lynn J. Gillard

Referee in Bankruptcy

Appendix B

United States Constitution Amendment V—Capital Crimes; Double Jeopardy; Self-Incrimination; Due Process; Just Compensation For Property

No person shall be . . . deprived of life, liberty or property without due process of law.

11 U.S.C. 41 (Bankruptcy Act Section 18(f)) . . . The filing of a voluntary petition under chapters 1 to 7 of this title, other than a petition filed in behalf of a partnership by less than all of the partners, shall operate as an adjudication with the same force and effect as a decree of adjudication.

11 U.S.C. 110 (Bankruptcy Act Section 70)

Title to property:

(a) The trustee of the estate of a bankrupt and his successor or successors, if any, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt as of the date of the filing of the petition initiating a proceeding under this title, except insofar as it is to property which is held to be exempt, to all of the following kinds of property wherever located . . . property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded, or sequestered. . . .

(d) After bankruptcy and either before adjudication or before a receiver takes possession of the property of the bankrupt, whichever first occurs—

(1) A transfer of any of the property of the bankrupt, other than real estate, made to a person acting in good faith shall be valid against the trustee if made for a present fair equivalent value or, if not made for a present fair equivalent value, then to the extent of the present consideration actually paid therefor, for which amount the transferee shall have a lien upon the property so transferred;

(2) A person indebted to the bankrupt or holding property of the bankrupt may, if acting in good faith, pay such indebtedness or deliver such property, or any part thereof, to the bankrupt or upon his order, with the same effect as if the bankruptcy were not pending;

(3) A person having actual knowledge of such pending bankruptcy shall be deemed not to act in good faith unless he has reasonable cause to believe that the petition in bankruptcy is not well founded;

(4) The provisions of paragraphs (1) and (2) of this subdivision shall not apply where a receiver or trustee appointed by a United States or State court is in possession of all or the greater portion of the non-exempt property of the bankrupt;

(5) A person asserting the validity of a transfer under this subdivision shall have the burden of proof. Except as otherwise provided in this subdivision and in subdivision g of section 44 of this title, no transfer by or in behalf of the bankrupt after the date of bankruptcy shall be valid against the trustee: *Provided, however,* That nothing in this title shall impair the negotiability of currency or negotiable instruments.